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Company update and
reco change

Pharmaceuticals

Target price: Rs954

Earnings revision

(%)	FY21E	FY22E	FY23E
Sales	-	-	32.7
EPS	-	-	94.7

Target price revision

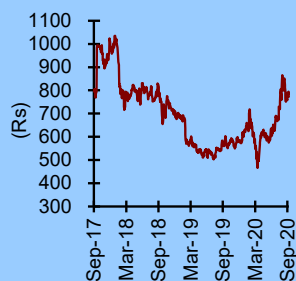
Rs954 from Rs875

Shareholding pattern

	Dec '19	Mar '20	Jun '20
Promoters	49.0	48.9	48.9
Institutional investors	31.6	32.3	33.3
MFs and others	7.9	8.5	8.7
Banks, FI's, Insurance co	1.1	1.1	0.2
FII's	22.6	22.7	24.4
Others	19.4	18.8	17.8

Source: BSE India

Price chart



INDIA

Natco Pharma

BUY

Upgrade from *Add*

Natco to launch first generic *Revlimid*

Rs776

Natco Pharma (Natco) would be the first company to launch *Revlimid* (lenalidomide) in Mar'22 as Dr Reddy's (DRL) settlement with Celgene over its patent clears the path for Natco. DRL would launch sometime after Natco (we assume 6 months) and would have market share restrictions lower than Natco in our view. Till date, three companies (Natco, DRL and Alvogen) have settled the litigation with innovator and would launch during this exclusivity period (FY23-FY26). We expect Natco to generate total revenue and PAT of US\$1.3bn and US\$900mn during the shared exclusivity period over FY23-FY26. This would imply an NPV of Rs302/share for *Revlimid* for Natco. Upgrade to BUY.

- **Certainty emerges on *Revlimid* launch:** After DRL's settlement with Celgene over *Revlimid* patent litigation, clarity has emerged on Natco's launch. Natco would now launch in Mar'22 and will have ~6months of head start before competitor's (DRL) launch. We also believe that Natco would have superior market share restrictions as compared to other players. As per Natco's settlement with Celgene, it can launch generic *Revlimid* in Mar'22 with mid-single digit market share constraint in first year which can gradually increase to ~33% in final year of exclusivity (FY26). Post Jan'26, there would not be any market share constraint.
- **Value *Revlimid* opportunity at Rs302/share:** The annual market size of this product is ~US\$8bn. Teva is the marketing partner for Natco and we assume Natco's share in the opportunity to be around 35%. Considering the factor of market share constraint, we believe pricing pressure would not be significant. We value *Revlimid* opportunity for Natco at Rs302/share.

	FY23E	FY24E	FY25E	FY26E	Total
Market Size (US\$ mn)	8,000	8,000	8,000	8,000	
Months	12	12	12	10	
Price erosion	20%	30%	40%	45%	
Market share	5%	15%	25%	33%	
Natco's sales (US\$ mn) assuming 35% share	112	294	420	508	1,334
PBT (US\$ mn)	101	265	357	432	
PAT (US\$ mn)	79	206	278	337	900
PAT in Rs m	5,897	15,479	20,885	25,270	67,531
EPS (Rs)	32	85	115	139	371
Years	1	2	3	4	
NPV (discount rate of 12%)	31	72	86	93	282
Value of recurring sales post FY26					20
Total value (Rs)					302

- **Valuations and risks:** We raise FY23 revenue/EPS estimates by 32.7/94.7% to factor in generic *Revlimid* sales. Considering certainty on *Revlimid* opportunity and 38.0% EPS CAGR over FY20-FY23E, we upgrade Natco to **BUY** from *Add* with a revised SoTP-based target price of Rs954/share (earlier: Rs875/share) including NPV of Rs302/share for *Revlimid*. Key downside risks: Delay in US launches and earlier-than-anticipated competition in *Copaxone*.

Market Cap	Rs141bn/US\$1.9bn
Reuters/Bloomberg	NATP.BO /NTCPH IN
Shares Outstanding (mn)	182.1
52-week Range (Rs)	898/450
Free Float (%)	51.1
FII (%)	24.4
Daily Volume (USD/'000)	4,271
Absolute Return 3m (%)	25.9
Absolute Return 12m (%)	36.2
Sensex Return 3m (%)	17.0
Sensex Return 12m (%)	8.0

Year to Mar	FY20	FY21E	FY22E	FY23E
Revenue (Rs mn)	19,150	21,145	23,325	33,945
Net Income (Rs mn)	4,608	4,925	5,647	12,103
EPS (Rs)	25.3	27.1	31.0	66.5
% Chg YoY	(28.5)	6.9	14.7	114.3
P/E (x)	30.6	28.7	25.0	11.7
CEPS (Rs)	39.9	30.8	33.4	38.1
EV/E (x)	24.6	21.9	19.0	8.8
Dividend Yield (%)	0.7	0.7	0.8	1.7
RoCE (%)	11.7	11.5	12.0	22.2
RoE (%)	12.7	12.4	12.9	24.0

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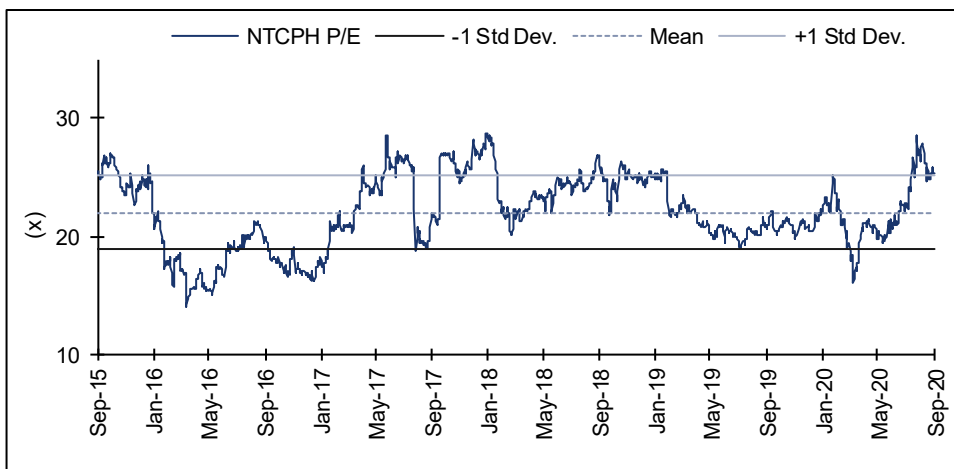
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Valuations

The stock currently trades at valuations of 25.0x FY22E and 11.7x FY23E earnings and EV/EBITDA multiple of 19.0x FY22E and 8.8x FY23E. We remain positive on long-term outlook driven by its strong US pipeline including opportunities like *Revlimid* & *Imbruvica*, recovery in domestic business in FY21E, potential upside in its agro business and targeted approach in RoW markets. Considering certainty on *Revlimid* opportunity and 38.0% EPS CAGR over FY20-FY23E, we upgrade Natco to **BUY** from *Add* with a revised SoTP-based target price of Rs954/share (earlier: Rs875/share) including NPV of Rs302/share for *Revlimid*.

Chart 1: 1-year forward P/E



Source: Company data, I-Sec research

Financial summary (Consolidated)

Table 1: Profit & loss statement

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
Domestic formulations	3,552	4,262	4,689	5,158
Export formulations	5,405	5,541	6,146	6,734
APIs	9,334	10,397	11,451	20,910
Other Operating Income	859	945	1,039	1,143
Total Gross Sales	19,150	21,145	23,325	33,945
Excise duty	-	-	-	-
Total Net Revenue	19,150	21,145	23,325	33,945
yoy Growth%	(8.6)	10.4	10.3	45.5
Total Op. Exp.	13,324	14,655	15,868	18,150
EBITDA	5,826	6,490	7,458	15,795
Margins %	30.4	30.7	32.0	46.5
yoy Growth%	(26.7)	11.4	14.9	111.8
Depreciation	998	1,148	1,281	1,440
EBIT	4,828	5,341	6,177	14,356
Other Income	1,074	1,128	1,218	1,315
Interest	215	190	190	190
EO Items	0	0	0	0
PBT	5,687	6,280	7,205	15,481
Tax	1,106	1,382	1,585	3,406
Tax Rate (%)	19.4	22.0	22.0	22.0
Minority Interest	(27)	(27)	(27)	(27)
Reported PAT	4,608	4,925	5,647	12,103
Adj. PAT	4,608	4,925	5,647	12,103
Net Margins (%)	24.1	23.3	24.2	35.7

Source: Company data, I-Sec research

Table 2: Balance sheet

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
Paid-up Capital	364	364	364	364
Reserves & Surplus	37,371	41,111	45,399	54,588
Total Equity	37,735	41,475	45,763	54,952
Minority Interest	112	85	58	31
Total Debt	3,159	3,159	3,159	3,159
Deferred Liabilities	259	259	259	259
Capital Employed	41,265	44,978	49,239	58,401
Current Liabilities	4,613	5,476	5,934	7,965
Total Liabilities	45,878	50,454	55,173	66,366
Net Fixed Assets	21,024	23,876	26,595	29,156
Investments	836	836	836	836
Inventory	5,580	6,137	6,645	7,601
Debtors	5,513	6,087	6,715	9,772
Other Current Assets	12,440	11,735	12,057	13,627
Cash and Equivalents	485	1,782	2,324	5,374
Total Cur. Assets	24,018	25,742	27,742	36,375
Total Assets	45,878	50,454	55,173	66,366

Source: Company data, I-Sec research

Table 3: Cashflow statement

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
PBT (Adj. for Extraordinary)	5,687	6,280	7,205	15,481
Depreciation	998	1,148	1,281	1,440
Net Chg in WC	(410)	(483)	(912)	(3,124)
Taxes	(1,078)	(1,382)	(1,585)	(3,406)
Others	(1,239)	920	(88)	(428)
CFO	3,958	6,483	5,901	9,963
Capex	(3,365)	(4,000)	(4,000)	(4,000)
Net Investments made	530	-	-	-
Others	1,165	-	-	-
CFI	(1,670)	(4,000)	(4,000)	(4,000)
Change in Share capital	58	-	-	-
Change in Debts	(809)	-	-	-
Div. & Div Tax	(1,536)	(1,185)	(1,359)	(2,913)
Others	(2,136)	-	-	-
CFF	(4,423)	(1,185)	(1,359)	(2,913)
Total Cash Generated	(2,135)	1,297	542	3,050
Cash Opening Balance	2,795	660	1,957	2,499
Cash Closing Balance	660	1,957	2,499	5,549

Source: Company data, I-Sec research

Table 4: Key ratios

(Year ending March 31)

	FY20	FY21E	FY22E	FY23E
Adj EPS	25.3	27.1	31.0	66.5
YoY Growth%	(28.5)	6.9	14.7	114.3
Cash EPS	39.9	30.8	33.4	38.1
EBITDA - Core (%)	30.4	30.7	32.0	46.5
NPM (%)	24.1	23.3	24.2	35.7
Net Debt to Equity (x)	0.1	0.0	0.0	(0.0)
P/E (x)	30.6	28.7	25.0	11.7
EV/EBITDA Core (x)	24.6	21.9	19.0	8.8
P/BV (x)	3.7	3.4	3.1	2.6
EV/Sales (x)	7.5	6.7	6.1	4.1
RoCE (%)	11.7	11.5	12.0	22.2
RoE (%)	12.7	12.4	12.9	24.0
RoIC (%)	12.5	11.9	12.7	24.1
Book Value (Rs)	207	228	251	302
DPS (Rs)	5.1	5.4	6.2	13.3
Dividend Payout (%)	20.0	20.0	20.0	20.0
Div Yield (%)	0.7	0.7	0.8	1.7
Asset Turnover Ratio	0.4	0.4	0.4	0.6
Avg Collection days	101	100	100	89
Avg Inventory days	104	101	100	77

Source: Company data, I-Sec research

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